

OFFICE OF AUDITS & ADVISORY SERVICES



COUNTY AIRPORT FISCAL CONTROLS – MCCLELLAN- PALOMAR

FINAL AUDIT REPORT

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August 13, 2012

TO: Richard E. Crompton, Director
Department of Public Works

FROM: Julie B. Nieminski
Chief of Audits

FINAL REPORT: COUNTY AIRPORT FISCAL CONTROLS – MCCLELLAN-PALOMAR

Enclosed is our report on the County Airport Fiscal Controls – McClellan-Palomar audit. We have reviewed your responses to our recommendations and have attached them to the audit report.

The actions taken and/or planned, in general, are responsive to the recommendations in the report. As required under Board Policy B-44, we respectfully request that you provide quarterly status reports on the implementation progress of the recommendations. The Office of Audits & Advisory Services will contact you or your designee near the end of each quarter to request your response.

Also attached is an example of the quarterly report that is required until all actions have been implemented. To obtain an electronic copy of this template, please contact Lindsey Heeszel at (858) 495-5576.

If you have any questions, please contact me at (858) 495-5661.

JULIE B. NIEMINSKI
Chief of Audits

AUD:LCH:aps

Enclosure

- c: Sarah Aghassi, Deputy Chief Administrative Officer, Land Use and Environment Group
Donald F. Steuer, Chief Financial Officer
Tracy M. Sandoval, Assistant Chief Financial Officer/Auditor and Controller
Kathleen Flannery, Group Finance Director, Land Use and Environment Group

INTRODUCTION

Audit Objective	<p>The Office of Audits & Advisory Services (OAAS) completed an audit of the County Airport Fiscal Controls – McClellan-Palomar. The objective of the audit was to review the fiscal controls and procedures of the McClellan-Palomar Airport in accordance with established laws, regulations, and County policy.</p>
Background	<p>The County operates eight airports, all of which are managed by Department of Public Works (DPW). This audit focused on the McClellan-Palomar Airport (Palomar Airport).</p> <p>The Palomar Airport is a single runway airport on approximately 480 acres in Carlsbad, California. The Palomar Airport provides commuter, business, private, and general aviation services.</p> <p>Currently, United Express is the only regularly-scheduled commercial airline flying out of the Palomar Airport. There are also eight Fixed-base Operators (FBOs) located at the Palomar Airport. A FBO is a commercial business that operates on an airport and provides aeronautical services such as fueling, aircraft parking and storage, aircraft rental, flight training, etc. These FBOs enter into long-term leases with the County in order to operate from the Palomar Airport. The Palomar Airport also has leases with other businesses such as car rental companies and a restaurant.</p> <p>The Palomar Airport relies on grant funding from the Federal Aviation Administration for approximately 95% of all approved capital improvement projects. The DPW employees who handle the leasing, invoicing, and grants for the Palomar Airport are also responsible for the County's other seven airports (DPW-Airports).</p>
Audit Scope & Limitations	<p>The scope of this audit focused on the adequacy of the fiscal controls and procedures of the Palomar Airport.</p> <p>This audit was conducted in conformance with the International Standards for the Professional Practice of Internal Auditing prescribed by the Institute of Internal Auditors as required by California Government Code, Section 1236.</p>
Methodology	<p>OAAS performed the audit using the following methods:</p> <ul style="list-style-type: none">• Interviewed key personnel on policies, procedures, and processes relevant to the areas being reviewed;• Examined policies and procedures related to the areas being reviewed and mapped key processes to obtain an understanding of the fiscal controls;

- Assessed the risks to achieving Palomar Airport's key objectives, with regard to fiscal controls, independently and in coordination with Palomar Airport and DPW management; and
- Conducted specific audit procedures (e.g., interviews, document inspections, and recalculations) on the following processes:
 - Grants;
 - Leases;
 - Fuel invoicing; and
 - Lease invoicing.

AUDIT RESULTS

Summary

Within the scope of the audit, there is reasonable assurance that the fiscal controls and procedures of the Palomar Airport are adequate. To further strengthen current controls and improve their effectiveness, OAAS has the following findings and related recommendations.

Finding I:

Reported Gross Revenue by Lessee is Not Fully Supported

Currently there are three lessees that report their total monthly revenues in order for the County to calculate their monthly "percentage of revenue" billings due to the County. OAAS noted during the audit that DPW-Airports' staff receive and accept only the total monthly revenue figure reported by the lessee without detailed supporting documentation. As a result, the audit testing could not confirm that County issued invoices that are based on a percentage of monthly gross revenue are in fact accurate and complete.

As a best practice, total revenue reported should be supported by all relevant types of revenue to ensure the total figure used to calculate the monthly billing is accurate and complete.

Recommendation:

To strengthen controls and ensure the accuracy of revenue billed and received by the County, DPW-Airports should:

1. Going forward, revise the percentage of income lease agreement (CCSF 85.23, rev. 6/00) Article 4 "Rent" to include that detailed reports of monthly revenue be provided with the gross revenue amount reported to the County.
2. Develop and implement internal procedures to ensure that the gross revenue amount reported is accurate and includes all relevant types of revenue as outlined in the lease.

Finding II:

Approved Variances to Insurance Requirements are Not Always Documented

The insurance requirements stated in each lease are not always consistent with the current insurance needs. Leases are often written for a long term period (up to 40 years) and the insurance requirements are drafted to be broad enough to change as the business changes.

However, when the actual insurance requirements differ from what is stated in the lease, DPW-Airports does not always maintain documentation of the approval or justification for this variance.

DPW-Airports' staff were able to provide support for all variances observed; however, it took considerable staff time to collect all documentation.

As a best practice, any variations from the lease requirements should be documented and signed by all parties and kept in the lease file as evidence that the variance is agreed to by all parties.

Recommendation: To strengthen controls related to insurance documentation, DPW-Airports should:

1. Implement an internal checklist for each lease file to verify an annual review was conducted, summarize any variances, and help organize the supporting documentation.
2. Review the checklists annually to ensure all updates and changes are approved by Risk Management and DPW-Airports, as appropriate.
3. Maintain documentation in the lease file of requests and approvals for all variance to the insurance requirements stated on the lease.

Office of Audits & Advisory Services

C Compliance R Reliability E Effectiveness A Accountability T Transparency E Efficiency

VALUE

DEPARTMENT'S RESPONSE



County of San Diego

RICHARD E. CROMPTON
DIRECTOR

DEPARTMENT OF PUBLIC WORKS

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OFFICE OF AUDITS &
ADVISORY SERVICES

Date: August 7, 2012

TO: Julie B. Nieminski, Chief of Audits
Auditor & Controller (O-305)

FROM: Richard E. Crompton, Director
Department of Public Works (O-332)

DEPARTMENT RESPONSE TO AUDIT RECOMMENDATIONS: AUDIT OF COUNTY AIRPORT FISCAL CONTROLS – MCCLELLAN-PALOMAR

Finding I: Reported Gross Revenue by Lessee Not Fully Supported

OAAS Recommendation: To strengthen controls and ensure the accuracy of revenue billed and received by the County, DPW-Airports should:

1. Going forward, revise the percentage of income lease agreement (CCSF 85.23, rev. 6/00) Article 4 "Rent" to include that detailed reports of monthly revenue be provided with the gross revenue amount reported to the County.
2. Develop and implement internal procedures to ensure that the gross revenue amount reported is accurate and includes all relevant types of revenue as outlined in the lease.

Action Plan: DPW agrees with the Audit recommendations and will take the following steps to address findings:

1. Airports will revise Article 4 "Rent" of existing leases that contain percentage rent provisions to require detailed reports of revenue be provided with the gross revenue amount reported to the County as each lease is renewed or amended. Airports will also include this requirement in any new percentage rent leases.
2. In the meantime, Airports Property Agents will (a) work cooperatively with Lessees to identify reports they can readily produce to ensure that the gross revenue includes all relevant types of revenue as outlines in the lease and includes detailed supporting documentation; (b) develop and implement procedures to regularly verify the detail supporting documents accurately agree or reconcile to reported gross revenue.

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Planned Completion Date:

1. For the three existing percentage rent leases revision of Article 4 "Rent" will be revised upon termination or amendment of the existing leases. This is expected to be February 1, 2016 for car rental leases and July 23, 2018 for the restaurant lease. This will also be included in any new percentage rent leases upon commencement.
2. Airports staff will (a) complete work with Lessees to identify reports Lessee can readily provide to document and support reported gross revenue by December 31, 2012; (b) complete and implement written procedures to evaluate and verify reports by January 31, 2013.

Contact Information for Implementation: Lee Ann Lardy, Project Manager-Airports Real Estate

Finding II: Approved Variances to Insurance Requirements Not Always Documented

OAAS Recommendation: To strengthen controls related to insurance documentation, DPW-Airports should:

1. Implement an internal checklist for each lease file to verify an annual review was conducted, summarize any variances, and help organize the supporting documentation.
2. Review the checklist annually to ensure all updates and changes are approved by Risk Management and DPW-Airports, as appropriate.
3. Maintain documentation in the lease file of requests and approvals for all variance to the insurance requirements stated on the lease.

Action Plan: DPW agrees with the Audit recommendations and will take the following steps to address findings:

1. Airports staff will revise its procedures to implement an internal checklist to be used to verify annual review is conducted and summarize any variances.
2. Airports staff will coordinate on the initial checklist with Risk Management and review annually with Risk Management to gain approval for any needed updates or changes to the checklist.
3. As each insurance certificate is received for leases staff will review, using the checklist as a tool to assist and document. The completed checklist will be filed under the insurance tab in the lease files in order to maintain appropriate documentation.

Planned Completion Date:

1. An updated written procedure will be completed by October 31, 2012.
2. Checklist will be developed and coordinated with Risk Management by November 30, 2012.

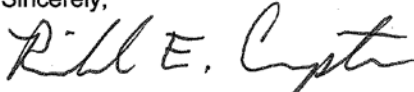
Ms. Nieminski
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3. Checklist for each lease will be completed and filed at each lease's annual insurance renewal and will be completed for all leases by November 30, 2013.

Contact Information for Implementation: Lee Ann Lardy, Project Manager-Airports Real Estate

If you have any questions, please contact Denbigh Dickson at (858) 874-4019 or Lee Ann Lardy at (619) 956-4824.

Sincerely,



RICHARD E. CROMPTON, Director
Department of Public Works

cc: Denbigh Dickson – Department of Public Works
Lee Ann Lardy – Department of Public Works